Dundee College

Annual Report to the Board of Management and the Auditor General for Scotland 2010/11

December 2011

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Executive Summary

Finance

Our audit of Dundee College is complete and our audit opinions on the truth and fairness of the financial statements and the regularity of transactions are unqualified.

The College has reported a deficit of £2.532m in 2010/11. This includes exceptional restructuring costs of £1.563m incurred as a result of a substantial staff restructuring exercise during 2010/11. The College undertook this exercise in response to the funding pressures it is facing, and expects to undertake further restructuring in 2011/12 to meet ongoing funding pressures.

The College's latest FFR projects a surplus of £4.008m in 2011/12, although this expected to be achieved after a substantial gain on sale of assets (£1.709m) and revaluation reserve transfer. The operating surplus on continuing operations is expected to be a more modest £30,000.

Governance

The College's Corporate Governance Statement confirms that the College has been compliant with the key principles of the UK Corporate Governance Code during 2010/11. We have reviewed the College's statement and can confirm that this is in line with the SFC's guidance and is not inconsistent with our understanding of the College's governance arrangements based on the information gathered as part of our normal audit work. Internal audit have made a series of recommendations in their 2010/11 Corporate Governance review, to further develop arrangements within the College, and we endorse these measures.

We did not identify any areas of concern from our review of the College's corporate governance arrangements in so far as they relate to prevention and detection of fraud and irregularity or standards of conduct and prevention and detection of corruption.

Conclusion

This report concludes the 2010/11 audit of Dundee College. We have performed our audit in accordance with the Code of Audit Practice published by Audit Scotland, International Standards on Auditing (UK and Ireland) and Ethical Standards.

This report has been discussed and agreed with the Assistant Principal & Director of Finance. We would like to thank all members of the College's management and staff who have been involved in our work for their co-operation and assistance during our audit.

Scott-Moncrieff
19 December 2011

Introduction

1. This report gives a summary of the findings from our audit of Dundee College ("the College") in 2010/11. The scope of our audit was set out in our External Audit Strategy and Plan which was presented to College management in June 2011. Our audit has focused on the financial statements and governance arrangements at the College.

2. We identified the following key issues in relation to the 2010/11 audit:

   - Estate developments and asset construction
   - Tayside Superannuation Fund (TSF) accounting
   - The College's financial position
   - Early retirement liabilities.

3. This report includes our findings in relation to these key issues.

4. The report is also addressed to the Auditor General for Scotland and will be published on Audit Scotland's website, www.audit-scotland.gov.uk.

Finance

5. This section of the report summarises our findings in relation to the College's financial performance for the year and its position at 31 July 2011. We also discuss any significant issues identified during our audit.

6. It is the responsibility of the College to conduct its financial affairs in a proper manner. It is our responsibility to audit the financial statements and to consider the College's governance arrangements in relation to the College's financial position.

Auditors' opinion

7. We are required to give an opinion as to whether the financial statements present a true and fair view of the financial position of the College as at 31 July 2011 and of its expenditure and income for the financial year. We are also required to include a regularity assertion in our independent auditors' report stating whether, in all material respects, expenditure and income were incurred or applied for their intended purposes and in accordance with guidance issued by the Scottish Ministers and the financial memorandum with Scottish Funding Council (SFC).

8. Our audit is now complete and we have issued unqualified audit opinions on the truth and fairness of the accounts and on the regularity of transactions.

9. The signed financial statements will now be submitted to Audit Scotland, who will pass them to the Scottish Government for laying before the Scottish Parliament.

Financial position

The College has reported a deficit of £2.532m for the year to 31 July 2011, with significant restructuring costs incurred

10. The College has reported a deficit of £2.532m in 2010/11. This includes exceptional restructuring costs of £1.563m incurred as a result of a substantial staff restructuring exercise during 2010/11. The College undertook this exercise in response to the funding pressures it is facing, and expects to undertake further restructuring in 2011/12 to meet ongoing funding pressures.

11. To address the financial challenges faced by funding reductions, the College is looking to significantly increase the level of charitable and philanthropic-type donations in 2011/12 and beyond. These donations are often made to support specific projects and areas of activity. The Statement of Recommended Practice: Accounting for Further and Higher Education (SORP 2007), coupled with the SFC model set of accounts, sets out specific accounting guidance in this area. The exact treatment will be determined by the specific conditions attached to the donation. For example, this may lead to donations being classed as restricted funding, required to be separately identifiable within the College's accounts.

12. The College will have to ensure that these funds are administered and accounted for properly. This can have various implications, including the need to maintain sufficient and appropriate accounting records for any endowments and ensuring appropriate banking/investment tracking arrangements are put in place.

Action plan point 1

Balance sheet

The College continues to report a strong balance sheet, including £40.052m of assets under construction

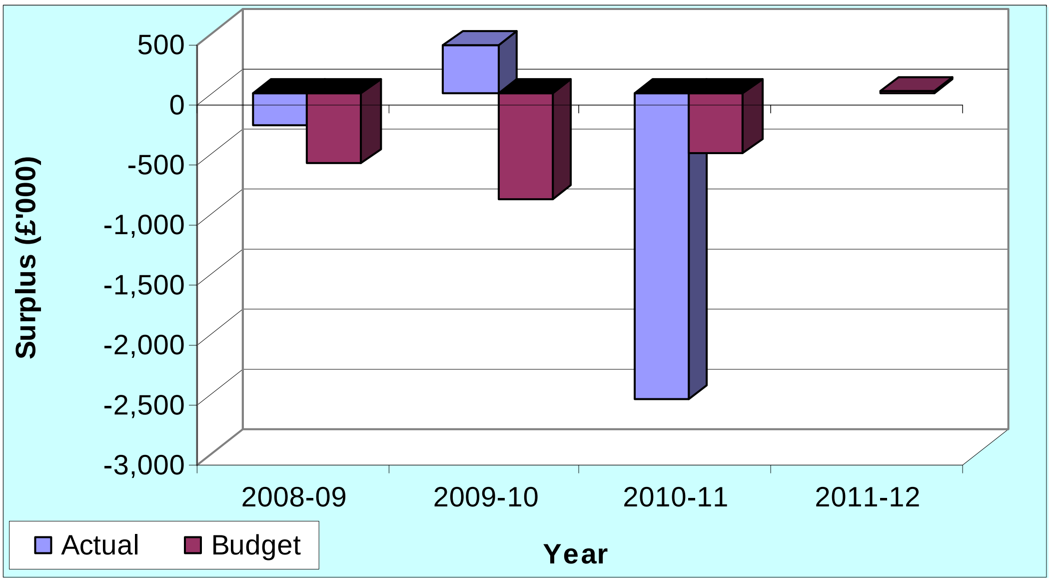
13. The College has reserves of £14.796m at 31 July 2011 (£17.328m as at 31 July 2010) and holds £40.279m of deferred capital grants (£22.583m at 31 July 2010). The reserves position has weakened due to the deficit which has been made in the year and further release from the revaluation reserve. The deferred capital grants position reflects the significant increase in assets under construction. There was also a healthy cash balance totalling £6.365m at year end, sourced via a long-term debt facility with Santander plc.

Financial forecasts

SFC funding has been confirmed for 2011/12 and a small operating surplus has been forecast, boosted by planned asset disposal. However, significant risk remains

14. The College has returned the 2011 Financial Forecast Return (FFR) to the Scottish Funding Council (SFC). SFC uses the FFR to assess the financial position and performance of individual colleges and the sector as a whole. SFC has confirmed funding for 2011/12, but, unlike previous years, the College has not been asked to provide three year projections given uncertainty over the financial position of the sector as a whole. This presents a significant risk, given the College's recent financial performance. The College should seek to formalise its medium term plans as soon as it receives clarity on funding from SFC. The ability of the College to retain the expected gain on asset disposals will be a significant element in the future financial performance of the College. Diagram 1 below compares the actual results with FFR forecasts and sets out projections for 2011/12.

Diagram 1 - Actual performance and FFR Forecasts



Source: Financial Forecast Returns, adjusted for 2011/12 to reflect operating surplus. Note: the FFR projections do not include potential further restructuring costs in 2011/12.

Financial planning and monitoring arrangements

The College continues to make difficult decisions to work towards a firmer financial footing

15. As part of our audit, we considered the College's financial standing, including the arrangements in place for financial planning, budgetary control and financial reporting. It is important that such arrangements are adequate in order to properly control the College's operations and use of resources.

16. College budgets are devised at the start of the year and approved by the Board of Management. These are reviewed during the year and updated to take account of new information. Management accounts are discussed by the Senior Management Team on a regular basis and presented to each of the quarterly Finance Committee meetings for review and comment.

17. The College expects to undertake further restructuring in 2011/12 to meet ongoing funding pressures.

Audit adjustments

18. During the course of our audit a small number of adjustments to the financial statements were identified and agreed. This had a small impact on the surplus, as management updated the draft accounts during and after the main audit visit. Changes were also made which were of a presentational and disclosure nature.

19. We also agreed a small number of adjustments to the balance sheet which did not impact directly on the surplus for the year. These included adjustment to european debtors, reclassification across categories in the balance and adjustment to depreciation (with offset from deferred capital grant).

20. There was one unadjusted audit difference, in relation to early retirements, which is discussed further below.

Early retirement provision

21. The College has previously offered early retirement to staff as part of the management restructuring programme. The College makes monthly payments to the pension fund to cover any shortfall arising from the decision to grant early access to retirement benefits. In line with *Financial Reporting Standard 12 - Provisions, Contingent Liabilities and Contingents Assets* (FRS 12), the College creates a provision for the future payments in relation to these early retirements. The provision for early retirement was £4.342m at 31 July 2011 (£4.433m at 31 July 2010).

22. In 2010/11 we identified an audit adjustment to reflect the change in those making up the early retirement provision, estimated at £120,000. As the College has not accepted this adjustment, we will append this to our letter of representation. This adjustment would reduce the provision on the balance sheet and decrease the deficit for the year.

Tayside Superannuation Fund liabilities

23. The College's employees belong to two principal defined benefit pension schemes, the Scottish Teachers' Superannuation Scheme (STSS) for the teaching staff and the Tayside Superannuation Fund (TSF) for the non-teaching staff.

24. The STSS is a multi-employer, notionally funded scheme and the College is unable to identify its share of the underlying assets and liabilities of the scheme. In line with FRS 17, the College has not recognised any asset or liability relating to STSS and the scheme is effectively accounted for as if it is a defined contribution scheme.

25. The TSF is also a multi-employer scheme. Following discussion in 2008/09 with Barnett Waddingham, the TSF actuary, we confirmed that the College is not currently able to identify its share of the scheme assets on a reasonable and consistent basis. This is because assets are allocated on a pro-rata basis every three years in proportion to the liabilities held at that time, and are not tracked on an ongoing basis. This has been further confirmed by the pension fund administration team at Dundee Council, who have confirmed in writing that the fund characteristics have not changed in either 2009/10 or 2010/11.

26. The College has not recognised any asset or liability relating to TSF and the scheme is effectively accounted for as if it is a defined contribution scheme. This is consistent with the approach taken in 2008/09 and 2009/10. We have reviewed the College's disclosure within the financial statements and considered the accounting treatment to be appropriate, given the basis of

allocation of scheme assets to the College. This is in line with our opinions in 2008/09 and 2009/10.

27. In our 2009/10 report, we noted that scheme assets could be tracked for the College (that is, at employer level), going forward. This has been confirmed by the scheme actuary. We again strongly recommended that the College continues to investigate this issue further with TSF and the scheme actuary, to consider if this has any implications for future FRS 17 accounting and reporting. There have been no notable developments during 2010/11 in this area. We acknowledge that the College is a minority stakeholder in the scheme.

Review of accounting and control systems

28. During our audit work we have considered the College's accounting systems and internal controls. We have made the following observation.

TSF employee contributions

29. We identified issues in our sample testing of superannuation contributions, regarding the accuracy of the percentage of employee contribution deducted and paid over to the Tayside Superannuation Fund for a group of employees. As an employee deduction, this does not impact directly on the College's accounts. However, the issue reflects a breakdown of procedures in the administration and control of the scheme and processes should be strengthened to ensure any adjustments to deduction rates are made in a timely manner.

Action plan point 2

Other issues of significance in the 2010/11 audit

Estates Strategy

30. The College has moved forward in 2010/11 with the significant plans to reconfigure its estate, from the current five site model to two main campuses at Kingsway and Gardyne. The Gardyne redevelopment is a £48.9m project, to be funded through a mix of SFC grant, asset disposal, College borrowing and existing cash resources. The Gardyne project is due for completion at the start of the 2011/12 academic year.

31. £26.797m of assets under construction were recognised in the College's balance sheet in the year to 31 July 2011, in addition to the £13.255m recognised in 2009/10.

32. We reviewed the College's plans and progress during our audit visit, including certified spend to the financial year end and the implications for the existing estate. We are satisfied that the College has accounted for the works appropriately.

33. In reviewing the accounting for the three College sites to be disposed of (Constitution Road, Graham Street and Melrose Terrace) we have obtained assurance regarding the values of these sites in the College's financial statements.

Governance

34. It is the College's responsibility to ensure that it has adequate governance arrangements in place. It is our responsibility to review and report on these arrangements as they relate to:

- the College's review of its systems of internal control, including reporting arrangements
- the prevention and detection of fraud and other irregularities
- standards of conduct and arrangements for the prevention and detection of corruption
- the College's financial position.

35. We reported on the corporate governance arrangements in relation to its financial position in the Finance section of this report. This section includes our comments on other aspects of the College's arrangements.

Corporate Governance

Appropriate governance arrangements are in place within Dundee College

36. Colleges are required to include in their annual accounts a statement covering the responsibilities of their Board of Management in relation corporate governance arrangements. The statement should describe the ways in which the College has complied with good practice in corporate governance, including the arrangements for risk management, and report on the College's compliance with the UK Corporate Governance Code.

37. The College's Corporate Governance Statement for 2010/11 states that the College was fully compliant with the UK Corporate Governance Code throughout the period.

38. We reviewed the Corporate Governance Statement by:

- checking the statement against SFC and Audit Scotland guidance
- considering the adequacy of the process put in place by the Principal and Board of Management to obtain assurances on systems of internal control
- assessing whether disclosures in the statement are consistent with our knowledge of the College.

39. We are satisfied that the statement is consistent with SFC and Audit Scotland guidance and that the contents are not inconsistent with information gathered during the course of our normal audit work. Internal audit have made a series of recommendations in their 2010/11 Corporate Governance review, to further develop arrangements within the College, and we endorse these measures.

The UK Corporate Governance Code has come in to effect for Colleges in 2010/11

40. A new Corporate Governance Code was published in June 2010 and has come in to effect for financial years beginning on or after 29 June 2010. The UK Corporate Governance Code, formerly known as the Combined Code, sets out standards of governance for listed companies. The Code is also applicable to publicly funded bodies that are required to prepare an annual statement on internal control or corporate governance for inclusion in their annual accounts. The "comply or explain" provision is retained in this new version of the code.

41. The College considered the implications of the new code, in line with our recommendation in our 2009/10 annual report. This review found that not all of the provisions within the Code were relevant to the College. The new code did not add materially to the existing corporate governance and risk management procedures already in place. This is in keeping with our cumulated understanding of the College's governance arrangements.

Risk management

The College has sufficient and appropriate risk management systems in place

42. The College continues to observe its approved Risk Management Framework and has a risk register in place. The Board of Management, with support from Executive Team, has overall responsibility for overseeing risk management. Risks are identified and assessed by the Executive Team and Strategic Forum and monitored by the Audit Committee.

43. From our review, the College appears to have sufficient and appropriate overall risk management systems in place.

Internal audit

44. The internal audit service is a key component of the College's internal control framework. As part of our corporate governance responsibilities, we have considered the College's arrangements to ensure that the work of internal audit is sufficient in quality and volume and complies with best practice. Our review was performed in accordance with the Code of Audit Practice and *International Standard on Auditing 610: Considering the work of internal audit* (ISA 610).

Considering the work of internal audit

45. We are committed to avoiding duplication of audit effort and ensuring an efficient use of the College's total audit resource. For 2010/11 the internal audit service has been provided by Henderson Loggie. We have considered internal audit findings as part of our audit and have sought to minimise duplication of effort, to ensure the total audit resource to the College is used efficiently and effectively.

46. Henderson Loggie have concluded in their annual report that Dundee College has adequate and effective internal control systems, with proper arrangements in place to promote and secure value

for money. We are grateful to Henderson Loggie for their ongoing assistance during the course of our audit work.

Prevention and detection of fraud and irregularity

47. As part of our audit we consider how the College ensures compliance with all relevant guidance and regulations. This includes a consideration of the College's arrangements for the prevention and detection of fraud and irregularity.

48. The College has a fraud prevention policy and fraud response plan. The College has also established processes for staff to raise concerns. Management confirmed that there were no frauds identified during the year.

49. All SFC and other guidance and regulations are recorded by the College, with records maintained to confirm action taken on each of the requirements of the circulars.

50. We identified no issues of concern in relation to the arrangements for the prevention and detection of fraud, with regard to the legality of transactions or in relation to compliance with relevant guidance and regulations.

Standards of conduct

51. We are required to consider the arrangements made by management in relation to standards of conduct and prevention and detection of corruption. Propriety requires that public business is conducted with fairness and integrity. This includes avoiding personal gain from public business, being even-handed in the appointment of staff, letting contracts based on open competition and avoiding waste and extravagance. Guidance on standards of conduct, accountability and openness has been issued by the Scottish Government.

52. Our work in this area included a review of the arrangements for adopting and reviewing standing orders, financial instructions, registers of interest and schemes of delegation and complying with national and local codes of conduct. Our audit identified no issues of concern in relation to standards of conduct, integrity and openness.

Looking Forward

Financial position

53. There is increasing uncertainty over the level of future funding that will be provided to the sector. Indications from the Scottish Government are that the reductions in funding experienced in 2010/11 may continue over the next few years. Coupled with increasing cost pressures this will result in significant financial challenges for the College and the sector as a whole.

54. SFC has confirmed funding for 2011/12, but, unlike previous years, the College has not been asked to provide three year FFR projections given uncertainty over the financial position of the FE and public sector as a whole. This puts pressure on the College's ability to plan its medium term financial future. It is undoubtedly a significant variable which complicates strategic decision making.

International financial reporting standards

55. The College's financial statements are still prepared on the basis of UK accounting standards (UK GAAP) which the Statement of Recommended Practice: Accounting for Further and Higher Education (SORP) Board believes continues to be appropriate for colleges.

56. Colleges will continue to converge with international financial reporting standards (IFRS) as UK GAAP converges with IFRS. It appears likely that full implementation of IFRS will not take place before 2013/14.

57. As we have previously noted, the conversion process requires sufficient and appropriate information to be available to support the production of comparator balances. Effectively, this means work to produce full IFRS-compliant financial statements will begin at least one year before the actual implementation date. In some areas, such as in relation to fixed assets and component accounting, the earlier the work begins the more straightforward the conversion process may be and we endorse any moves the College may make to work towards IFRS transition in a structured and well-planned way.

Appendix 1 – Action Plan

Our annual report action plan details the financial control weaknesses and opportunities for improvement that we have identified during our audit visit in addition to any reportable matters arising from our review of performance and governance systems.

The action plan details the officers responsible for implementing the recommendations and implementation dates. The College should assess these recommendations for their wider implications before approving the action plan. Following submission of this report to the Audit Committee, we will send a copy to the Auditor General.

It should be noted that the weaknesses identified in this report are only those that have come to our attention during the course of our normal audit work. The audit cannot be expected to detect all errors, weaknesses or opportunities for improvements in management arrangements that may exist.

Grading

To assist the Board in assessing the significance of the issues raised and prioritising the action required to address them, the recommendations have been graded. The grading structure is summarised as follows:

Grade 5	Very high risk exposure - Major concerns requiring Board attention.
Grade 4	High risk exposure - Material observations requiring management attention.
Grade 3	Moderate risk exposure - Significant observations requiring management attention.
Grade 2	Limited risk exposure - Minor observations requiring management attention
Grade 1	Efficiency / housekeeping point.

Issues arising from our 2010/11 audit

No	Title	Issue identified	Risk and recommendation	Management comments
1	**Donation accounting** **(Para 12)**	There may be specific accounting requirements which the College must follow in relation to substantial charitable and philanthropic-type donations being sought in 2011/12 and beyond.	There is a risk of non-compliance with accounting requirements. The College should ensure that these funds are administered in line with the SORP and applied in line with the conditions of any award. Areas for specific consideration include maintaining sufficient and appropriate accounting records for any endowments and putting appropriate banking/investment arrangements in place. **Grade 2**	Noted and agreed. **Responsible officer:** Assistant Principal & Director of Finance and Head of Finance **Implementation date:** 31 December 2011

No	Title	Issue identified	Risk and recommendation	Management comments
2	**Superannuation Administration** **(Para 29)**	We identified issues in our sample testing of superannuation contributions, regarding the accuracy of the percentage employee contribution deducted and paid over to the Tayside Superannuation Fund for a group of employees. As an employee deduction, this does not impact directly on the College's accounts. However, the issue reflects a breakdown in procedures in the administration and control of the scheme.	Incorrect contributions could adversely impact on the employee's position with TSF. Processes should be strengthened to ensure any adjustments to superannuation contribution rates are made in a timely manner. The College should ensure all issues relating to any previous incorrect deductions are resolved with TSF. **Grade 2**	Noted and agreed. **Responsible officer:** Assistant Principal & Director of Finance and Head of Finance **Implementation date:** Ongoing

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